



Signed and Filed: December 27, 2010

*Dennis Montali*

DENNIS MONTALI  
U.S. Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT  
NORTHERN DISTRICT OF CALIFORNIA

In re	)	Bankruptcy Case
	)	No. 09-33549DM
RAY K. SHAHANI,	)	
	)	
Debtor.	)	Chapter 11
	)	
RAY K. SHAHANI, individually and as	)	Adversary Proceeding
TRUSTEE OF THE 888 TRUST DATED	)	No. 10-3022DM
AUGUST 10, 2006,	)	
	)	
Plaintiff,	)	
	)	
v.	)	
	)	
UNITED COMMERCIAL BANK, et al.,	)	
	)	
Defendants.	)	

MEMORANDUM DECISION FOLLOWING TRIAL

I. INTRODUCTION.

Plaintiffs Ray K. Shahani and the 888 Trust (together "Shahani") brought this action for breach of a construction loan agreement, wrongful foreclosure, damages and other relief in the San Francisco Superior Court against East West Bank as assignee from the FDIC as Receiver for United Commercial Bank (both referred to herein interchangeably as "Bank") and other defendants. After Ray K. Shahani filed Chapter 11 on November 11, 2009, he removed it to this court on February 24, 2010.

The court issued a Temporary Restraining Order and later on

1 May 10, 2010, a Preliminary Injunction (the "Injunction")  
2 prohibiting Bank from disposing of the real property at 888  
3 Airport Blvd. in Burlingame, CA (the "Property").

4 The matter was tried to the court on September 20 & 21, 2010,  
5 and thereafter the parties submitted simultaneous post-trial  
6 written arguments. The court took the matter under submission and  
7 on November 8, 2010, issued its Preliminary Ruling Following  
8 Trial. In that ruling the court noted that pivotal to the  
9 resolution here is the issue of whether Shahani or Bank first  
10 breached the March 16, 2007, Construction Loan Agreement between  
11 United Commercial Bank and the 888 Trust (the "CLA"). If Shahani  
12 did, the Bank's non-performance thereafter is excused; if Bank  
13 did, Shahani might well be entitled to set aside the foreclosure  
14 sale or recover damages.

15 Shahani thereafter asked to submit further argument and the  
16 court afforded both sides an opportunity to do so. Having  
17 considered those additional arguments, the court adheres to its  
18 preliminary ruling and will enter judgment in favor of Bank.

19 II. DISCUSSION.<sup>1</sup>

20 Under the CLA, Bank loaned \$2,025,000 to pay off an existing  
21 loan on the Property and finance the construction of an office  
22 building on it. Bank's commitment under the CLA was to finance  
23 the completion of what the parties have described as the warm  
24 shell of the building, not the final improvements.

25 The loan was evidenced by a promissory note and secured by a  
26 deed of trust with the usual terms for enforcement in the event of

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28 <sup>1</sup>The following discussion constitutes the court's findings of  
fact and conclusions of law. Fed. R. Bankr. P. 7052(a).

1 a default. The original due date of the note was April 5, 2008.

2 During the course of construction Shahani chose to develop  
3 and construct more improvements on the Property than were  
4 contemplated by the CLA. He advanced \$533,000 for those  
5 additional improvements. Shahani selected Scott General, Inc.  
6 ("Scott") as the general contractor on the project. Bank selected  
7 an independent third party inspection company, Cardinal  
8 Consulting, Inc. ("Cardinal") to monitor progress on the project,  
9 including verifying percentages of completion in response to  
10 periodic draw requests.

11 By May, 2008, Scott became concerned about Shahani's ability  
12 to pay for the additional improvements he was adding beyond those  
13 covered by the CLA. When Shahani was unable to supply Scott with  
14 evidence of an ability to pay for those improvements, Scott  
15 abandoned the project on May 22, 2008, asserting that it was owed  
16 approximately \$196,000 in unpaid fees and costs.

17 When presented with Draw Request No. 10, Cardinal reviewed  
18 the progress of the project, including the difficulties with Scott  
19 that included a mechanic's lien Scott recorded against the  
20 Property on June 5, 2008. Cardinal recommended responding to Draw  
21 Request No. 10 by having Bank release an amount limited to  
22 approximately \$118,600, or roughly 60% of that claimed by Scott in  
23 its mechanic's lien.<sup>2</sup> Shahani contends that Bank breached the CLA  
24 by denying payment of Draw Request No. 10 and that had it honored  
25 that request he could have satisfied Scott and saved the project.  
26 Bank countered by arguing that Scott's abandonment on May 22,

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28 <sup>2</sup>Scott recorded a second mechanic's lien a few weeks  
thereafter.

1 constituted an event of default under section 25.18 of the CLA,  
2 namely if its borrower ceases construction on the Property.  
3 Further, section 25.16 of the CLA provides the an event of default  
4 occurs if any default continues beyond any applicable cure period.  
5 Bank also contends that Scott's recording of the mechanic's liens  
6 against the Property constituted two independent defaults under  
7 section 25.10 of the CLA. Shahani contends that had Scott been  
8 paid the \$118,600, it would not have pursued its mechanic's liens  
9 remedies.<sup>3</sup> The court rejects this argument as unfounded and pure  
10 speculation.

11 Shahani also contends notwithstanding the problems with Scott  
12 and the recorded mechanic's liens, that Bank extended the maturity  
13 date of the note from October 5, 2008, until January, 2009, and  
14 thus its recording of a notice of default on January 29, 2009, was  
15 premature. Shahani relies on a December 10, 2008, e-mail from  
16 Bank officer Leonard Woolfolk ("Woolfolk") stating, "the loan is  
17 being extended through January, 2009." The court agrees with Bank  
18 that at the time of the Woolfolk e-mail, the loan was already in  
19 default and there was nothing to extend. Further, there were no  
20 contractual agreements or discussions about any definitive terms  
21 of such an extension. In any event, a few days after the Woolfolk  
22 e-mail Bank informed Shahani in writing that the amounts due under  
23 the loan were due and payable and Shahani expressed no concern  
24 about any purported extension of the loan.

25 Bank recorded its notice of default on January 29, 2009, just  
26 two days prior to the date Shahani contends was an extended  
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28 <sup>3</sup>Shahani ultimately settled with Scott in August, 2009.

1 maturity of the Note. Because the sale did not occur until  
2 October 1, 2009, Shahani had ample time to pay off the entire  
3 amount due under the loan as permitted by California Civil Code §  
4 2924(f).

5       Following trial the Bank appears to have abandoned its  
6 contentions about Shahani's abandonment of the project, and with  
7 good reason. Woolfolk was crystal clear in his belief that  
8 Section 25.18 applied, and repeatedly stressed that Scott's  
9 walking off the project was a breach by Shahani. It is crystal  
10 clear that he was incorrect. Had Shahani terminated Scott,  
11 Woolfolk would have been correct, but that is not what happened.  
12 For section 25.18 to apply, Shahani would have had to abandon the  
13 project. He did not. Thus there were not two extant breaches oof  
14 the CLA as of June 5, 2008; there was one, the recorded mechanic's  
15 lien, but it was material enough to excuse Bank from funding Draw  
16 Request No. 10. The second mechanic's lien added another breach  
17 of the CLA.

18       Shahani cannot avoid or defend those breaches. As  
19 persuasively argued by Bank in its post-trial brief, it would  
20 require too much speculation for the court to conclude that had  
21 Bank paid approximately \$118,000 on June 6 (or June 10,  
22 recognizing that Bank was entitled to a response to a June 3 e-  
23 mail asking for more details regarding how Shahani was dealing  
24 with Scott) that Scott would have removed its first lien and not  
25 recorded its second one. While perhaps not Shahani's fault  
26 (except to the extent he could not provide Scott with financial  
27 assurances), Scott's conduct led to the conditions described in  
28 Exhibits A and F (see Bank's post-trial brief at 5:9-19) excusing

1 Bank's further performance.

2 On other issues presented, the court agrees with Bank. The  
3 January 29, 2009, Notice of Default was not premature. Bank did  
4 not violate a duty of good faith and fair dealing. Bank's offer  
5 to accept a discount in full satisfaction of its note upon  
6 Shanhan's refinancing of the project through Private Funding  
7 Solutions, Inc., by a deadline expired before the refinancing  
8 could be accomplished, and Bank was under no legal obligation to  
9 extend that deadline. The exchange of e-mails and voicemail  
10 messages in the final hours before the sale did not invalidate the  
11 foreclosure sale and had no effect on the outcome.

12 Because the court is ruling in favor of Bank it does not need  
13 to address whether Debtor, Ray K. Shahani, has standing to  
14 prosecute this action when the Property was owned by the 888  
15 Trust.

16 Bank is entitled to a dissolution of the Injunction and entry  
17 of a judgment in its favor for the reasons set forth in this  
18 memorandum decision. Each side should bear their own costs.  
19 Bank's counsel should serve and upload such a judgment, and comply  
20 with B.L.R. 9021-1.

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22 \* \* \* END OF MEMORANDUM DECISION \* \* \*  
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